[COMMITTEE PRINT]

ENERGY TAX ACT OF 1977

SECTION-BY-SECTION DESCRIPTION OF TITLE II OF H.R. 6831

AS REPORTED BY THE

COMMITTEE ON WAYS AND MEANS

PREPARED FOR THE

AD HOC COMMITTEE ON ENERGY
HOUSE OF REPRESENTATIVES

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

JULY 19, 1977

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1977

93-242 O

JCS 41-77

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Residential energy credit—Section 44C of the Code

(a) A credit is allowed to individuals for qualified energy conservation expenditures.

(b) The amount of qualified energy conservation expenditures for which the credit may be allowed is 20 percent of the first $2,000 of expenditures (a maximum credit of $400) made in the tax year.

The maximum expenditure amount is to be reduced by earlier expenditures which were taken into account in computing a credit for an earlier tax year in the credit period. Therefore, the maximum credit may be taken only once for each succeeding principal residence of the taxpayer. However, an individual will be eligible for the maximum credit each time he changes his principal residence, regardless of expenditures he made for a prior principal residence, and regardless of expenditures made by prior residents of his present principal residence.

For any credit to be allowed, a minimum credit amount of $10 is required with respect to each return (joint or separate). This minimum credit amount is for the combination of insulation and other energy-conserving component expenditures and for all solar and wind energy expenditures as well.

The credit is nonrefundable, i.e., it cannot exceed the individual's tax liability in the year for which the credit is claimed.

(c) To qualify for the credit, installations of insulation and other energy-conserving components must be in or on an individual's principal residence, and that residence must be located in the United States. The credit is available only for installations in or on residences the construction of which was substantially completed before April 20, 1977.

Qualifying insulation is an item specifically and primarily designed to reduce, when installed in or on a dwelling (or water heater), the heat loss or gain of the dwelling (or water heater). A qualifying energy-conserving component is any item (other than insulation) which is:

(1) a furnace replacement burner designed to achieve a reduction in the amount of fuel consumed as a result of increased combustion efficiency;

(2) a device for modifying flue openings designed to increase the efficiency of operation of the heating system;

(3) an electrical or mechanical furnace ignition system which replaces a gas pilot light;

(4) a storm or thermal window or door for the exterior of the dwelling;

(5) a clock thermostat;

(6) caulking or weatherstripping of an exterior door or window; or

(7) an item of a kind which the Secretary of the Treasury specifies by regulations as increasing the energy efficiency of the dwelling.

In the case of both insulation and other energy-conserving components, the original use of the property must commence with the taxpayer. Both must also be reasonably expected to remain in operation for at least three years and to meet performance and quality standards prescribed by the Secretary of the Treasury after consultation with the Secretary of Energy, Secretary of Housing and Urban Development, and other appropriate Federal agencies. These standards are not to apply to property purchased prior to the promulgation of the standards.

The Secretary of the Treasury may issue regulations specifying property which qualifies as insulation or as an energy-conserving component.

To qualify for the credit, expenditures for insulation or other energy-conserving components must be "made" during the credit period. Under the amendment, these expenditures are treated as "made" when the original installation of the insulation or other energy-conserving component is completed.

The entire cost of qualifying property is allowed toward the credit only if at least 80 percent of the property's use is for personal residential purposes. If less than 80 percent of the use of the property is for personal residential purposes, the amount of the expenditure which is allowable toward the credit is reduced proportionately. For purposes of this provision, use for a swimming pool is not treated as a personal residential purpose.

Under this provision, a dwelling is considered a taxpayer's principal residence during the 30-day period prior to the time it would otherwise be considered the taxpayer's principal dwelling. As a result, qualifying expenditures made by a taxpayer on a residence within 30 days of occupation of that residence as a principal residence will qualify for the credit.

(d) Qualifying expenditures by individuals jointly occupying a dwelling as their principal residence are apportioned toward the credit among those individuals as if they were one taxpayer. As a result, a total of $2,000 of qualifying expenditures may be made for their residence, rather than $2,000 for each of the occupants. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

Cooperative housing association stockholders and condominium management association members (as well as owners and renters) will all be eligible to claim the credit. The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's members' allocable share is to be the amount he is assessed by the association as a result of the insulation and other energy-conserving component expenditures.

(e) In order to avoid a double tax benefit (the credit plus a reduced gain on a subsequent sale of the residence), what would otherwise be an increase in the tax basis of the residence because of qualifying expenditures is to be reduced by the amount of the credit allowed for these expenditures.

(f) These amendments to the Internal Revenue Code of 1954 are to apply to taxable years ending on or after April 20, 1977, for expenditures considered made on or after that date and before 1983.

2. *Section 2011 of the committee amendment—Residential energy credit for solar and wind energy equipment*

Residential energy credit—Section 44C of the Code

(a) A credit is allowed to individuals for qualified solar and wind energy expenditures.

(b) The amount of qualified solar and wind energy expenditures for which the credit may be allowed is 30 percent of the first $1,500 of expenditures and 20 percent of the next $8,500 (a maximum credit of $2,150).

The maximum expenditure amount is to be reduced by earlier expenditures which were taken into account in computing a credit for an earlier tax year in the credit period. Therefore, the maximum credit may be taken only once for each succeeding principal residence of the taxpayer. However, an individual will be eligible for the maximum credit each time he changes his principal residence, regardless of expenditures he made for a prior principal residence, and regardless of expenditures made by prior residents of his present principal residence.

For any credit to be allowed, a minimum credit amount of $10 is required with respect to each return (joint or separate). This minimum credit amount is for the combination of all solar and wind energy expenditures and for all insulation and other energy-conserving component expenditures in a taxable year.

The credit is nonrefundable, i.e., it cannot exceed the individual's tax liability in the year for which the credit is claimed.

(c) To qualify for the credit, installations of solar and wind energy property must be in connection with an individual's principal residence, and that residence must be located in the United States. The credit is available for both existing and newly constructed dwellings.

Qualifying solar property is equipment which uses solar energy to heat or cool the dwelling or to provide hot water for use within the dwelling. Qualifying wind energy property is equipment which uses wind energy for personal residential purposes. Qualifying property does not include any swimming pool used as an energy storage medium, nor does it include any other energy storage medium which serves a dual purpose.

In the case of both solar and wind energy property, the original use of the property must commence with the taxpayer. Both solar and wind energy property must also be reasonably expected to remain in operation for at least five years and to meet performance and quality standards prescribed by the Secretary of the Treasury after consultation with the Secretary of Energy, the Secretary of Housing and Urban Development, and other appropriate Federal agencies. These standards will not apply to equipment purchased prior to the promulgation of the standards.

Qualifying expenditures include not only the cost of the solar or wind energy property itself, but also the costs of the onsite preparation, assembly, or installation of the property.

To qualify for the credit, solar and wind energy expenditures must be made within the credit period. These expenditures are generally treated as made when the original installation of the property is completed. However, in the case of solar and wind energy expenditures in connection with the construction or reconstruction of a dwelling, these expenditures are treated as made when the taxpayer commences original use of the dwelling as his principal residence.

The entire cost of a qualifying property is allowed toward the credit only if at least 80 percent of the property's use is for personal residential purposes. If less than 80 percent of the use of the property is for personal residential purposes, the amount of the expenditure which is allowable toward the credit is reduced proportionately. Use for a swimming pool is not treated as a personal residential purpose.

Under this provision, a dwelling is considered a taxpayer's principal residence during the 30-day period prior to the time it would otherwise start being considered the taxpayer's principal dwelling. As a result, qualifying expenditures made by a taxpayer on a residence within 30 days of occupation of that residence as a principal residence will qualify for the credit.

(d) Qualifying expenditures by individuals jointly occupying a dwelling as their principal residence are apportioned toward the credit among those individuals as if they were one taxpayer. As a result, a total of $10,000 of qualifying expenditures may be made for their residence, rather than $10,000 for each of the occupants. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

Cooperative housing association stockholders and condominium management association members (as well as owners and renters) will also be eligible to claim the credit. The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's member's allocable share is to be the amount he is assessed by the association as a result of the solor and wind energy expenditures.

(e) In order to avoid a double tax benefit (the credit plus a reduced gain on a subsequent sale of the residence), what would otherwise be an increase in the tax basis of the residence because of qualifying expenditures is to be reduced by the amount of the credit allowed for these expenditures.

(f) These amendments to the Internal Revenue Code of 1954 are to apply to taxable years ending on or after April 20, 1977, for expenditures considered made on or after that date and before 1983.

B. Provisions Relating to Transportation

Section 2021 of the committee amendment—Gas guzzler tax

Gas Guzzler Tax—Section 4064 of the Code

(a) A gas guzzler tax would generally apply to automobiles which fall below the mandatory fleetwide automobile efficiency standards of present law (that is, from more than 3 miles per gallon to more than 5.5 miles per gallon, depending upon the year involved). The tax would apply to 1979 and later model year automobiles.

The amount of the tax applicable to an inefficient automobile would be prescribed in separate rate tables for each of the model years, 1979 through 1984, and the table for 1985 also would apply to all subsequent years. The tax would range from $339 to $553 for 1979 model year automobiles, $249 to $666 for 1980 model year automobiles, $245 to $1,216 for 1981 model year automobiles, $266 to $1,565 for 1982 model year automobiles, $345 to $2,134 for 1983 model year automobiles, and $397 to $3,856 (for an automobile rated below 12.5 mpg) for 1985 ant later model year automobiles.

(b) The gas guzzler tax generally applies to vehicles which are manufactured primarily for use on public streets, roads and highways and which are rated at 6,000 pounds gross vehicle weight or less. However, the tax would not apply to trucks with a cargo capacity of 1,000 pounds or more.

(c) The bill prescribes specific mileage standards and specific testing procedures (which are, in general, the same procedures that are currently followed by EPA). These standards and testing procedures are not tied to any changes which might be made by the Department of Transportation at a later time.

Reduction in basis of automobile on which gas guzzler tax was imposed—Section 1016(c) of the Code

A purchaser of an automobile subject to the gas guzzler tax would be required to reduce his basis in the automobile by the amount of the tax for all purposes, including depreciation, the investment credit and gain or loss on sale. This rule applies only if the vehicle is less than 1 year old when purchased.

Denial of exemptions and refunds—Sections 4221, 4293, and 6416 of the Code

The gas guzzler tax (unlike other manufacturers excise taxes) would apply to vehicles purchased by State and local governments and by tax-exempt educational institutions (without provision for refund). Also, the Secretary of the Treasury would not have the authority to waive the application of the tax to automobiles purchased by the United States Government.

Leases of automobiles subject to the gas guzzler tax—Section 4217(e) of the Code

If a manufacturer leases automobiles rather than sells them, the first lease would be treated as a sale and the gas guzzler tax would be collected in the portion that each lease payment bears to the total lease price.

Section 2022 of the committee amendment—Trust fund for purposes of reducing public debt

The proceeds of the gas guzzler tax would be appropriated to a newly created Public Debt Retirement Trust Fund which would be utilized to retire a portion of the national debt.

Section 2023 of the committee amendment—Repeal of deduction for State and local taxes on gasoline and other motor fuels

Repeal of deduction for State and local taxes on gasoline and other motor fuels—Section 164(a)(5) of the Code

The itemized deduction presently allowed for the State and local taxes imposed on gasoline and other motor fuels used for nonbusiness purposes would not be allowed for amounts paid or incurred after December 31, 1977.

Section 2024 of the committee amendment—Extension to 1985 of existing rate of tax on gasoline and other motor fuels

Extension to 1985 of existing rate of tax on gasoline and other motor fuels—Sections 4041, 4081, and 6421 of the Code

The current Federal excise taxes of 4 cents per gallon imposed on gasoline, diesel fuel, and certain special motor fuels, which were scheduled to be reduced to 1½ cents per gallon on October 1, 1979, would be extended through September 30, 1985.

Section 2025 of the committee amendment—Amendment of motorboat fuel provisions

Retailers excise tax on special motor fuels—Section 4041(b) of the Code

The retailers excise tax on special motor fuels (other than diesel) would be revised by providing that a full tax of 4 cents per gallon (rather than a special 2-cent-per-gallon rate) would apply to fuels sold for use in motorboats.

Partial refund of gasoline taxes for nonhighway use—Section 6421 of the Code

Under present law, gasoline is generally taxed at 4 cents per gallon, but a 2-cent-per-gallon-reduction is available, by way of credit or refund, for off-highway use. The Ways and Means Committee Amendment denies this refund or credit if the gasoline is used in a motorboat.

These provisions would become effective on October 1, 1977.

Section 2026 of the committee amendment—Removal of excise tax on buses

Excise tax on buses and trucks—Section 4063(a) of the Code

The 10-percent manufacturers excise tax on buses (which is reduced to 5 percent on October 1, 1979) is repealed for sales of buses occurring on or after April 20, 1977.

Section 2027 of the committee amendment—Removal of excise tax on bus parts and accessories

Exemptions for (or refunds of) excise tax on parts and accessories for buses—Section 4221(e)(6) and 6416 (b)(2) of the Code

The 8-percent manufacturers exise tax on bus parts (scheduled to be reduced to 5 percent on October 1, 1979) is repealed with respect to sales on or after the first day of the first calendar month beginning more than 10 days after the date of enactment. This provision is designed to provide either an exemption from the tax or a refund or credit of the tax in situations where parts (including parts which may be used interchangeably on a truck or a bus) are used on a bus.

Section 2028 of the committee amendment—Removal of excise taxes on certain items used in connection with certain intercity, local or school buses

Exemption from excise taxes on highway tires, inner tubes and tread rubber—Section 4221(e)(5) of the Code

The excise taxes on highway tires, inner tubes and tread rubber are not to apply to with respect to items used on intercity, local, and school buses.

Definitions of bus operations qualifying for exemptions—Section 4221(d)(7) of the Code

To qualify for the exemption from (or refund of) the taxes on tires, tubes, tread rubber, or lubricating oil, the items must be used on or in an "intercity or local bus" or a "school bus." An "intercity or local bus" is any bus which is used predominately (that is, more than 50 percent) in furnishing (for compensation) passenger land transportation available to the general public, if either (1) the transportation is scheduled and along regular routes, or (2) in the case of charter or other non-scheduled operations, the passenger seating capacity of the bus is at least 20 adults (not including the driver). A "school bus" means any bus with respect to which "substantially all" (that is, at least 85 percent) of the use involves transporting students and employees of schools.

Repayment of tax on lubricating oil in intercity, local, or school buses—Section 6424(a) of the Code

A credit or refund will be provided for the excise tax paid on lubricating oil used in intercity, local, or school buses (as defined above).

Refund of excise taxes on gasoline or other motor fuels for intercity, local, or school bus operations—Sections 6421(b) and 6427(b) of the Code

The taxes paid on gasoline and other motor fuels will be refunded to the extent these fuels are used in a bus engaged (1) in furnishing (for compensation) passenger land transportation available to the general public or (2) in school bus transportation operations. The allocation of fuel to these nontaxable uses may be determined on a mileage basis or on an actual fuel use basis. Use in "passenger land transportation available to the general public" means the same type of use that would qualify in meeting the predominate use test for intercity or local buses, and use in school bus transportation operations means the same type of use that would qualify in meeting the "substantially all the use" test for school buses.

Section 2029 of the committee amendment—Tax credit for qualified electric motor vehicles

Tax credit for qualified electric motor vehicles—Section 44D of the Code

A nonrefundable tax credit (i.e., the credit cannot exceed the taxpayer's tax liability) would be provided for the first $300 of the purchase price of a new electric motor vehicle (designed for highway operation) purchased by an individual for personal use on or after April 20, 1977 and before January 1, 1983. This credit applies only to new vehicles, not to used vehicles or vehicles converted to electricity.

C. Crude Oil and Natural Gas Liquids Equalization Taxes and Rebates

Section 2031 of the committee amendment—Crude oil equalization taxes

Imposition of tax—Section 4986 of the Code

(a) An excise tax is imposed on the first purchase of domestically produced crude oil. Only lower tier oil is subject to the tax in 1978 and 1979. Between 1980 and the termination date, all price-controlled oil is subject to the tax.

(b) In 1978, the tax on lower tier oil is $3.50 per barrel. In 1979, the tax on lower tier oil is the difference between the national average refiner acquisition cost of upper and lower tier oil. Between 1980 and the termination date, the tax on all controlled oil is equal to the difference between the controlled price of each classification of crude oil by grade, type and location and the uncontrolled price for that classification of crude oil. This rate of tax will generally increase the price of all controlled crude oil to what its uncontrolled price would be were there no price controls. However, in the case of "new new oil," the tax cannot exceed the difference between the uncontrolled price and the then highest controlled price for oil of the same classification.

(c) An excise tax is also imposed on the sale for end use of natural gas liquids after December 31, 1977, and before the termination date. Exemptions from the tax are provided for natural gas liquids that are used as feedstocks to produce natural gas liquid products and liquids used on a farm for farming purposes or in a church, residence, school or hospital.

(d) In 1978, the amount of the tax on controlled natural gas liquids is one third of the difference between the controlled price of the natural gas liquid and the wholesale price, by region, of No. 2 distillate oil, adjusted for the difference in Btu content of natural gas liquids and No. 2 distillate oil. (This difference is called "price gap.") In 1979, the tax is two-thirds of the price gap. In 1980 and thereafter, the tax is equal to the price gap.

(e) The taxes on controlled crude oil and natural gas liquids expire on September 30, 1981 (the "termination date").

Provisions of common application—Section 4987 of the Code

(a) The first purchaser of the controlled crude oil is liable for the crude oil equalization tax. Generally, the first purchaser must pay the tax. The tax is due by the first day of the fourth calendar month after the month of the first purchase. However, where the first purchaser is a nonresident alien not doing business in the United States, or in other cases where there is a substantial likelihood that the first purchaser will not pay the tax, the Secretary may provide by regulations for the collection of the tax from a subsequent purchaser.

(b) The natural gas liquids tax is imposed on the purchaser for end use and collected by the seller. The tax is payable on or before the 15th day of the second month after the sale for end use.

(c) Where crude oil is used to produce natural gas liquids, a credit or refund of the crude oil equalization tax is provided for the crude oil used to produce the natural gas liquids. The credit or refund is available only if the refiner establishes that the price of the natural gas liquids has not been increased by any portion of the crude oil equalization tax. For each barrel of crude oil used to produce natural gas liquids, the credit or refund equals the average per barrel crude oil equalization tax for all oil consumed in the United States.

(d) The President is granted standby authority to suspend any increase in the equalization taxes where he determines that the increase will cause a substantial adverse economic effect. However, either House of Congress can veto any suspension plan within 15 days of its submission to the Congress by the President. Moreover, no suspension can last for more than one year without additional Presidential action and additional Congressional approval.

Definitions and special rules—Section 4988 of the Code

(a) This section provides a number of definitions, including definitions of crude oil, natural gas liquids, and lower and upper tier crude oil. Generally, these definitions are similar to the definitions used for price control purposes. However, the definition of "new new oil" is not the price control definition. For purposes of the tax, "new new oil" is any oil produced from a property which was not in commercial production at any time during the 90-day period ending on April 20, 1977, and oil produced from any reservoirs which go into production after that date.

(b) The crude oil equalization tax applies only to crude oil produced in the United States including its possessions and the continental shelf. The natural gas liquids tax only applies to natural gas liquids sold or used in the United States.

(c) Where crude oil is refined, exported or otherwise used before its first purchase, the first purchase is deemed to occur at the time of removal from the lease. An exemption is provided for crude oil and certain refined products that are used on the lease for the extraction of crude oil or natural gas.

(d) A number of definitions are provided for determining uncontrolled price and controlled price. The controlled price is the ceiling price under price control regulations. The uncontrolled price is the price the oil would have sold for if there were no price controls. Where no uncontrolled price for a particular classification of crude oil is available for comparison, the Secretary is authorized to determine the uncontrolled price on the basis of the best available information. These determinations are to be made in such a way as to prevent undue hardships and windfalls.

(e) The tax applies proportionately to fractional barrels of oil or natural gas liquids.

Section 2032 of the committee amendment—Miscellaneous provisions

(a) *Study of small and independent refiners.*—This section requires the Secretary of Energy to conduct a study of the effect of the imposition of the crude oil equalization tax and any phaseout of the entitlements program on small and independent refiners and to present the report to Congress within 90 days after the date of enactment of the bill.

(b) *Effect of crude oil equalization taxes on certain natural gas contracts.*—This section provides that the crude oil equalization taxes shall not be taken into account in determining the price of natural gas under contracts entered into before the date of enactment of the bill.

Section 2033 of the committee amendment—Establishment of trust fund for the return of crude oil equalization taxes

(a) A trust fund is established for the return of equalization taxes on crude oil and natural gas liquids.

(b) The trust fund will receive the amount of the equalization taxes for 1978, less related reductions in income taxes arising from the imposition of the equalization taxes and less payments to refiners who produce natural gas liquids from crude oil.

(c) The trust fund can only be used for the return of equalization taxes as provided in the committee amendment.

(d) The trust fund terminates on December 31, 1979.

Section 2034 of the committee amendment—Per taxpayer credit of crude oil equalization tax receipts

Crude oil equalization tax receipts credit—Section 44E of the Code

(a) Generally, the equalization taxes are returned in the form of an income tax credit to all taxpayers for 1978. The amount of the credit will be reflected in the withholding tables.

(b) Joint returns and heads of households are entitled to twice the usual credit.

(c) The amount of the credit (called the "crude oil payment") is (1) the estimated amount of equalization taxes for 1978, less (2) the estimated loss in income taxes resulting from the imposition of the equalization taxes, and less (3) the estimated administrative costs, divided by (4) the estimated total number of crude oil payments. This will be the amount which causes all of the net revenues raised by the taxes to be returned to consumers.

(d) Except for persons entitled to the earned income credit, the credit may not exceed tax liability.

(e) Trusts, estates, and nonresident aliens are not eligible for the credit.

Section 2035 of the committee amendment—Special payments to recipients of benefits under social security, railroad retirement, and supplemental security income programs

Payments equal to the crude oil payment are to be made to each individual who received either a social security, railroad retirement, or supplemental security income check in June 1979. Child beneficiaries of social security (except disabled adult children) are excluded. This payment will be reduced by the amount of any crude oil equalization tax receipts credit allowed to the individual on his 1978 income tax return. These payments are to be made by September 1979 and are to be paid out of the trust fund.

Section 2036 of the committee amendment—Special payment to recipients of aid to families with dependent children under approved State plans

This section provides that a payment equal to the crude oil payment is to be made by the States to each parent or relative receiving aid to families with dependent children, with two payments being made where the individual is a head of household. (Child beneficiaries of AFDC are excluded.) These payments are to be made by September 30, 1979. The States will be completely reimbursed out of the trust fund for the costs (including administrative costs) of the payments.

Section 2037 of the committee amendment—Other special payments

The Treasury is required to pay to any resident adult (age 18 by December 31, 1978) who had not received the full crude oil payment as a credit or other payment the amount of his remaining crude oil payment. Heads of households are entitled to two payments. These individuals would claim their payment by filing a form with the Treasury.

Section 2038 of the committee amendment—Provisions applicable to special payments generally

This section provides rules to facilitate the making of the crude oil payments, including rules for the exchange of information to prevent double payments and relief from liability for Government officials where double payments are unavoidably made. The tax credits in excess of tax liability and the special payments are to be disregarded in determining eligibility for, or benefits under, Federal or Federally assisted aid programs.

Section 2039 of the committee amendment—Refunds of crude oil equalization taxes for residential, etc., use

Heating oil refund for residences, hospitals, schools, and churches—Section 6429 of the Code

This section provides for a refund of the crude oil equalization tax to retailers of heating oil that is used in a residence, hospital, church or school if the retailer establishes that his price to these consumers has not been increased by the crude oil equalization tax. Retailers of heating oil will receive advance payments in order to alleviate any hardship from paying higher prices for heating oil before they receive the refund.

Section 2040 of the committee amendment—Payments to Puerto Rico and the possessions of the United States

This section authorizes payments to the governments of Puerto Rico and the possessions of the energy payments for their residents contingent on these governments submitting an acceptable plan to the Secretary of the Treasury providing for the distribution of these amounts to their residents in a manner similar to the program applicable to residents of the United States.

D. Tax on Business Use of Oil and Gas and Credits

Section 2041 of the committee amendment—Excise tax on business use of oil and gas

Imposition of tax—Section 4991 of the Code

(a) An excise tax is imposed on each taxable use of oil and natural gas.

(b) The amount of the tax on oil is shown in the following table (the Tiers are defined in section 4993):

	The tax per barrel is—		
	Tier 1	Tier 2	Tier 3
If the taxable use occurs during calendar year—			
1979	$0.30	$0.30	None
1980	.60	.60	None
1981	1.00	1.00	None
1982	1.00	1.45	None
1983	1.00	2.00	$1.50
1984	1.00	2.50	1.50
1985 or thereafter	1.00	3.00	1.50

The tax for 1981 and each year thereafter is adjusted for inflation.

(c) The amount of tax per million BTU on Tier 1 and Tier 2 uses of natural gas is the excess of the applicable natural gas target price per million BTU over the user acquisition cost per million BTU. These terms are defined in section 4994.

The tax on a Tier 3 use of natural gas is not imposed for years before 1983. For 1983, the rate is $.55 per million BTU, for 1984, $.65, for 1985 and thereafter $.75; these rates are adjusted for inflation for 1981 and each year thereafter. The tax on Tier 3 use of natural gas is subject to a cap described in section 4994.

(d) The inflation adjustment is made by comparing the implicit price deflator for the gross material product for the preceding calendar year with the deflator for 1979.

(e) Taxes are to be rounded to the nearest whole cent.

(f) The tax for any calendar year shall be paid by the user.

(g) The tax is due on or before July 1 of the succeeding calendar year.

(h) If the President determines that the imposition of the tax would have an adverse economic effect, he may submit to the Congress a plan providing for the suspension of all or part of the tax for up to one year. This plan would have to describe the considerations which caused the President to propose the suspension. The suspension would take place only if neither House of Congress adopts a resolution of disapproval within 15 days of its submission.

Taxable use defined—Section 4992 of the Code

(a) Taxable use of oil or natural gas does not include any exempt use or the exempt amount.

(b) Exempt uses include use in residential facilities, use in a vehicle, aircraft, or vessel or in transportation by pipeline, use on a farm for farming purposes, use in a facility which is not an integral part of manufacturing, processing, or mining, and use in the exploration for, or the development, extraction, or storage of crude oil, natural gas, or natural gas liquids.

Exempt uses also include exempt process uses; this term does not include any use in a boiler or in a turbine or other internal combustion engine. It does include the use of oil or natural gas in any manufacturing process if there is no substitute fuel which may be used without materially and adversely affecting the manufacturing process or the quality of the manufactured goods, and the use of which is economically and environmentaly feasible.

Exempt use also includes use in certain facilities subject to air pollution regulations. If a facility was in existence or under construction on April 20, 1977 (or if on this date there was a binding contract for the construction of a facility), and the use of coal in this facility is precluded by Federal or State air pollution regulations, then the use of oil or natural gas in this facility is to be exempt from taxation. The State law exemption is only available, however, if State regulations precluding the use were in effect on April 20, 1977, or if the Secretary determines after consultation with appropriate Federal and State agencies, that the adoption of the State regulations are necessary to meet a requirement of Federal law. Regulations of any local agencies which have jurisdiction under a Federally approved State Implementation Plan would also be taken into account if these regulations were in existence on that date or they are necessary to meet a requirement of Federal law.

(c) The exempt amount for the taxpayer for any calendar year is the BTU content of 50,000 barrels of oil. Persons who are members of the same controlled group of cooperations and trades or business (whether or not incorporated) which are under common control are to be treated as one taxpayer. If the taxpayer owns a plant and there are other facilities in the same region which are competitive with the plant which have no users tax liability because of the exempt amount, and if the tax liability on the taxpayer's plant would result in a substantial competitive disadvantage to the taxpayer, then the Secretary is to provide an additional exempt amount for this plant to the extent necessary to alleviate the competitive disadvantage.

Tiers of tax, downward reclassification—Section 4993 of the Code

(a) The taxable uses of oil and gas are classified by tiers according to their level of tax. Tier 1 applies to process uses in which conservation of fuel is feasible. Tier 2 includes any use in a boiler or in a turbine or other internal combustion engine (not covered in Tier 3).

Tier 3 applies to electric utilities, as well as any other production of electricity using generating facilities with a rated capacity of at least 100 megawatts.

(b) Uses may be reclassified downward by the Secretary of the Treasury to a lower tier tax or an exempt use category on a temporary or permanent basis. Reclassifications can be made only after consultation with appropriate Federal agencies and only if it is determined that the reclassification is not inconsistent with the goals of conserving oil and gas or converting to other fuels.

(c) Temporary reclassifications to an exempt use category are to be granted to new electric power plants, new major fuel burning installations and cogenerating facilities which are granted exemption or exceptions from the coal conversion requirements of the Energy Supply and Environmental Coordination Act of 1974 (ESECA) (as amended by this bill) for the duration of their ESECA exemptions or exceptions.

Amount of natural gas tax—Section 4994 of the Code

(a) The natural gas target price per million BTU applicable to gas used in any region is the BTU equivalency price for this region minus the taxable use adjustment.

(b) The taxable use adjustment is a number from the following table (adjusted for inflation beginning in 1981 as specified in section 4991):

	The amount subtracted for Tier 1 is—	The amount subtracted for Tier 2 is—
If taxable use occurs during calendar year—		
1979	$1.35	$1.05
1980	.70	.40
1981	.65	.35
1982	.55	.25
1983	.50	.20
1984	.45	.15
1985 or thereafter	.30	Zero

(c) The Btu equivalency price for any calendar year for any region is to be based on the average regional price per barrel of all No. 2 grade distillate oil sold in the region during the preceding calendar year, but does not include the Section 4991 tax on this oil.

(d) The user acquisition cost per million Btu for any person is the average cost of natural gas for any use. In the case of natural gas which is used by gas producers or by any business under common control with the producer, or which was not acquired in an arm's-length transaction, the user acquisition cost is not to exceed the maximum lawful price applicable to a sale by the producer of such natural gas under the law of the United States. User acquisition cost does not include increases in State user taxes after April 20, 1977, but does include a reasonable allowance for transportation costs, not to exceed the cost which would be incurred in an arm's-length transaction.

(e) For Tier 1 or Tier 2 gas purchased under an interruptible contract, the applicable tax is to be reduced by 10 percent.

(f) The Tier 3 tax is subject to a cap, so that the tax cannot bring the cost of gas used for Tier 3 purposes above the Btu equivalency price of residual fuel oil, including the section 4991 tax imposed on such oil.

(g) The Secretary of the Treasury, after consultation with the Secretary of Energy, is to divide the United States into appropriate regions for purposes of this tax.

Definitions and special rules—Section 4995 of the Code

Oil means crude oil, refined petroleum products, and natural gas liquids, but does not include natural gas and gasoline. Natural gas includes natural gas, petroleum, or a product of natural gas or petroleum which has an API gravity of 110 or more. Neither oil nor natural gas is defined to include any substance of a kind not generally marketable for use as a fuel.

Section 2051 of the committee amendment—Credits against tax on business use of oil and gas

Allowance of credit—Section 4996

(a) A credit is allowed for investments in qualifying alternative energy property which may be offset directly against the oil and gas consumption tax liability.

(b) The Secretary of the Treasury may prescribe regulations to carry out the purposes of the credit.

(c) No credit shall be allowed for any calendar year after 1990 except to the extent of any carryovers arising from qualifying investments made in years prior to 1991 and for expenditures for property the physical construction, reconstruction or erection of which began before January 1, 1991.

(d) The credit against the users tax is allowed only where the taxpayer has made an election pursuant to section 4999(a) between the users tax credit or the energy tax credit.

Amount of credit—Section 4997

(a) The credit is an amount equal to 100 percent of the qualified energy investment for the calendar year but cannot exceed the users tax.

(b) Qualified energy investment generally is the cost of alternative energy property, referred to as "section 4996 property" placed in service by the taxpayer during the calendar year together with the qualified progress expenditures for such property during the year. The credit is limited to the users tax liability for the calendar year, but any excess investment may be carried forward and treated as qualified energy investment for the following calendar year.

(c) The credit for any calendar year is limited to the users tax for that year. The users tax for 1979 and for 1980 (including any tax carried forward from 1979) in excess of the qualified energy investment for each such year may be carried forward and treated as a users tax imposed in the following year. Where any credit is allowed in 1980 or 1981 solely as a result of the tax carryover from the previous year, the credit so allowed shall be treated as an overpayment.

(d) With regard to the treatment of the credit for ratemaking purposes, rules similar to the existing rules under section 46(f) relating to the investment credit shall apply. The Secretary is to prescribe rules to carry out the purposes of this provision including rules with respect to the time and manner of making elections similar to the elections described in section 46(f).

(e) Where the qualified energy investment is financed by the proceeds of any industrial development bond, the interest on which is tax exempt by reason of section 103, only 50 percent of the investment is to be taken into account in determining the amount of the credit against the users tax.

Section 4996 property—Section 4998

(a) The credit is allowable for investments in alternative energy property facilitating the use of fuels other than oil and gas, provided that the property is (1) new; (2) is used in the taxpayer's trade or business; (3) is eligible for depreciation (or amortization); (4) has a useful life of 3 years or more; and (5) is not used predominantly outside the United States.

(b) Alternative energy property is defined to include certain boilers; burners; advanced technology equipment for nuclear, hydroelectric, or geothermal power; gasification equipment; pollution control equipment; handling equipment for fuels other than oil and gas; and plans and designs for such equipment. A partial credit may be claimed for certain boilers which reduce their oil and gas use to at least 25 percent but not more than 50 percent of their total fuel.

Special rules—Section 4999

(a) The election to take the credit must be made on the taxpayer's income tax return for his first taxable year ending after December 31, 1978 in which the taxpayer has qualified energy investment. Once an election is made, it applies to all taxable years. It may be revoked only with the consent of the Secretary or his delegate. The election shall be effective for all qualified energy investment made by the taxpayer.

Where the taxpayer has made an election to take the credit against the users tax with respect to any qualifying energy investment, no energy investment credit against the income tax will be allowed, and the regular investment credit would be allowed only to the extent that current year's investment exceeds the tax for the year, and only if, the taxpayer elects to forego any carryover of the excess investment against the users tax which may be imposed in a later year. A regulated public utility has until its first taxable year ending after December 31, 1982 in which it has qualifying energy investment to make the election.

(b) For purposes of these rules, the taxpayers under common control include all members of the same controlled group of corporations as that term is defined in section 1563, but with a 50-percent control test (instead of 80 percent), together with other entities, whether or not incorporated, which are under common control. The Secretary shall prescribe rules consistent with the principles of section 1563 in applying the control test.

(c) Rules similar to the rules of the regular investment credit are provided for recapturing the credit where qualifying property is disposed of or ceases to be qualifying property within 7 years from the time the property is placed in service by the taxpayer.

(d) In the case of a regulated public utility (as defined in section 7701(a)(33)) whose principal activity is the sale of electricity, a credit shall be allowed for a boiler only to the extent that a boiler, which was in existence on April 20, 1977, and used oil or natural gas as its primary fuel on that date, is replaced or phased down. A boiler shall be treated as phased down only where the boiler was used more than 1500 hours in 1976 and will not be used more than 1500 hours in any year following the year in which the new boiler is placed in service (or after 1983 where the new boiler was placed in service before 1983).

Utilities may treat qualified progress expenditures as qualifying investment for any calendar year where the utility certifies to the Secretary or his delegate that the eventual replacement or phase-down of the old boiler will occur in the year following the year in which the new boiler is placed in service, provided the new boiler is to be placed in service within 3 years after the end of the first year for which the certification is effective.

Further, the bill provides that where a taxpayer has treated a new boiler as qualifying investment and subsequently the phased down boiler is used more than 1500 hours but not more than 2000 hours, the taxpayer's users tax on the oil or gas used in the additional hours shall be double the normal users tax. In the case of oil, the tax would be $3 per barrel ($1.50 regular tax and $1.50 additional tax). The additional tax would not be eligible for the rebate and could not be reduced by reason of the 50,000 barrel exempt amount (discussed above in connection with the tax.) If the phased-down boiler is used more than 2000 hours, the new boiler is to be treated as having been disposed of in the year in which that excess use occurs and the normal disposition rules will apply.

(e) No income tax deduction is available for the amount of the tax offset by the credit.

E. Business Energy Tax Credit; Investment Credit and Depreciation Changes

Section 2061 of the committee amendment—Changes in business investment credit and depreciation rules

a. Business energy investment credit (secs. 2061(a) and 2061(c))

A special 10-percent investment credit against income tax liability is provided to business and industry (including agriculture) for investments in certain types of energy-related property made after April 19, 1977 and before January 1, 1983.

This 10-percent business energy investment credit is in addition to the regular investment credit, which is presently also at a rate of 10 percent but which is scheduled to decline after 1980 to 7 percent generally, 4 percent for utilities. The business energy credit is available only where qualifying property is used in connection with a building or structure located in the United States. The property must have been completed or acquired by the taxpayer after April 19, 1977 and before January 1, 1983, and the credit generally applies to the costs incurred during this period. In order to qualify the property must also be new property subject to depreciation and which has a useful life of 3 years or more.

Definitions of energy property

Qualifying energy property is defined to include alternative energy property, that is, the same group of equipment which is eligible for the business oil and natural gas use tax credit. A taxpayer may elect either the use tax credit or business energy tax credit for alternative energy property. If a taxpayer elects the use tax credit, he may claim the regular investment credit against that part of his investment in alternative energy property which is not offset by the use tax credit. If the taxpayer elects the energy investment credit for alternative energy property, the credit may be used against all the taxpayer's income tax liability. The same rules apply to the replacement or phase-down of an electric utility boiler that apply for purposes of the use tax credit.

Eligible energy property also includes property which allows a taxpayer to make more efficient use of his available energy resources by cogenerating, that is both to generate electricity and to provide some other useful form of energy, such as steam, by adding equipment to expand or to create cogenerating capacity in an existing facility. Equipment which uses solar, geothermal and wind energy is made eligible for the credit, as is a variety of industrial heat recovery equipment to recapture and use otherwise wasted heat and gas. The other categories of eligible property are equipment used exclusively to recycle solid waste and equipment which enables a facility to reduce consumption of oil or natural gas as a fuel or feedstock by at least 25 percent by also using coal, waste, or some other material.

Except for alternative energy property and recycling equipment, the business energy credit generally will apply only to energy property used in connection with a building (or industrial process, where applicable) in existence on April 20, 1977. All categories of energy property other than alternative energy property must also satisfy performance and quality standards set by the Secretary of the Treasury.

The rate of the energy investment credit will be reduced to 5 percent where any qualifying property is acquired with the proceeds of a tax-exempt industrial development bond.

b. Investment credit for business insulation (sec. 2061(b))

Business insulation will be treated as qualifying property under the regular investment credit (presently 10 percent; 7 percent after 1980) for the period from April 20, 1977 through December 31, 1982. For this purpose, insulation means property which meets standards for reducing heat loss or gain set by the Secretary of the Treasury, including structural insulation, insulating glass, and storm doors and windows.

In order to qualify, the insulation must be used in a building or facility placed in service before April 20, 1977. In addition, it must be new property which has an estimated useful life of at least 3 years. The credit is reduced for insulation with a useful life of less than 7 years.

c. Limitations on investment credit and depreciation for certain property (sec. 2061(d) and (e))

Under this provision, the regular investment credit is denied for portable air conditioners and heaters, which tend to use energy inefficiently. Similarly, the investment credit and rapid depreciation (under accelerated methods and shortened useful lives) are also denied for new oil and gas boilers and other combustors placed in service after June 20, 1977, in those cases where the taxpayer is not prevented by State or Federal air pollution regulations from burning coal as a fuel and where this use of oil or natural gas is not an exempt use for purposes of the oil and natural gas use tax.

d. Rapid depreciation for retired or replaced oil and natural gas combustors (sec 2061(f))

Under this provision, where a taxpayer expects to retire or replace an existing oil or gas boiler or other combustor before the end of its useful life, the taxpayer's unrecovered costs for this combustor may be depreciated over this shortened period. In order to qualify for this provision, the taxpayer must establish to the satisfaction of the Secretary of the Treasury that this early retirement will in fact occur. If the early retirement does not occur by the expected date, the taxpayer is required to repay, with interest, any tax benefit it realized through increased depreciation deductions under this provision.

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F. Energy Tax Incentives

Section 2071 of the committee amendment—Intangible drilling costs for oil and gas wells

Section 2071 of the committee amendment extends for all future years the minimum tax provision (essentially, a 15-percent tax imposed on specified items of tax preference) on intangible drilling costs currently applicable for 1977. As a result, intangible drilling cost deductions for oil and gas wells (i.e., generally expenditures made by the owner of an operating interest in an oil or gas well for wages, fuel, repairs, hauling, supplies, etc. incurred in preparing a drill site, drilling and cleaning a well, and constructing assets which are necessary in drilling the well and preparing it for production, such as derricks, pipelines and tanks) would be included in the minimum tax base of individuals only to the extent that those costs, over the amount of those costs amortizable on the basis of a 10-year life, exceed the taxpayer's income from oil and gas properties. The amount of any excess intangible drilling costs would constitute a tax preference item and be subject to the minimum tax.

Section 2072 of the committee amendment—Intangible drilling costs for geothermal resources

(a) *Deduction of costs*

Section 2072(a) of the committee amendment provides taxpayers with the option to deduct currently, rather than to capitalize, intangible drilling and development costs related to the exploration for, and the development of, geothermal resources to the same extent and in the same manner as those expenses are deductible in the case of oil and gas wells. Geothermal deposits are defined broadly by the bill to mean geothermal reservoirs consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure).

(b) *Application of minimum tax*

Section 2072(b) of the committee amendment provides that the excess of the intangible drilling and development costs over the amount of those costs which would have been amortizable on the basis of a 10-year life and which further exceeds the taxpayer's income from the production of geothermal resources constitutes a tax preference for purposes of the minimum tax. Income from geothermal properties would have to be computed separately from the calculation of income from oil and gas properties. In general, the effect of this provision would be to apply the minimum tax to these deductions only with respect to investors who are not engaged actively in geothermal energy production.

(c) *Gain on sale or other disposition of geothermal property*

Section 2072(c) of the committee amendment provides that gain realized on the disposition of geothermal properties is subject to recapture (i.e., treated as ordinary income rather than capital gain) to the extent the gain does not exceed the amount by which the intangible drilling cost deductions exceed the amount of those deductions which would have been allowable had the costs been capitalized and deducted through cost depletion. Current law applies this rule to gain realized on the disposition of oil and gas properties.

(d) *Deduction of losses*

Section 2072(d) of the committee amendment provides that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, geothermal resources cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year (i.e., generally the amount of an otherwise allowable loss for the year cannot exceed the taxpayer's basis reduced by any nonrecourse borrowing to which the property is subject), as determined under existing law (sec. 465 of the Code). The purpose of this section of the bill is to prevent a taxpayer from deducting a loss in excess of his economic investment in a geothermal property.

Section 2073 of the committee amendment—Percentage depletion for geothermal resources

Section 2073 of the committee amendment provides a 10-percent allowance for percentage depletion for all geothermal resources, regardless of whether the resource would qualify for depletion under present law or whether the resource in fact is renewable. However, the amount of allowable depletion with respect to any property in any year may not exceed the taxpayer's adjusted cost basis in that property. Thus, once the taxpayer has recovered the cost of the property, through any combination of deductions or basis adjustments, no depletion deductions are allowable.

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G. Rerefined Lubricating Oil

Section 2074 of the committee amendment—Excise tax on rerefined lubricating oil

Section 2074 of the bill exempts the sale of new lubricating oil from the 6-cents-per-gallon manufacturer's excise tax where the lubricating oil is sold for use in mixing with previously used or waste lubricating oil which has been cleaned, renovated, or refined. For the exemption to apply, the blend of oil and new oil must consist of 25 percent or more of waste or refined oil. All of the new oil in a mixture is to be exempt from the excise tax if the blend contains 55 percent or less new oil. If the mixture contains more than 55 percent new oil, the excise tax exemption applies only with regard to the portion of the new oil that does not exceed 55 percent of the mixture.

H. Annual Report on Energy and Revenue Effects of the Energy Tax Provisions

Section 2075 of the committee amendment—Annual report on energy and revenue effects

The committee amendment requires the President to submit an annual report to the Congress every August after 1977. The report is to provide estimates of the amount of revenue increases or decreases resulting from each of the provisions of this bill and an evaluation of the extent to which each of the provisions has resulted in increased energy conservation and production.

The committee amendment also requires that the President provide such other information as he determines is relevant for an evaluation of the provisions of the bill. The committee report states that the Committee on Ways and Means expects the President to include in his report the petroleum (or natural gas) savings resulting from each provision and the extent to which shifts from petroleum and natural gas to other materials has occurred as a result of each provision.

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